No. 20,966

IN THE

United States Court of Appeals

For the Ninth Circuit

RICHARD L. CHARTRAND,
Appellant,

vs.

BARNEY'S CLUB, INC., a Nevada corporation,
Appellee.

Appeal from the United States District Court for the District of Nevada

APPELLANT'S REPLY BRIEF

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SUMMARY OF REPLY ARGUMENT

Appellant acknowledges that he is bound by the lower court's findings of facts and does not dispute such findings. Apparently Appellee misconceives the nature of these findings for the trial court's finding was not to the effect that since the corporation received the benefits of the pre-incorporation contract knowledge of the contract would thereby be imputed to it. The lower court's finding was that the corporation had knowledge of the terms of the agreement prior to its acceptance of the benefit because O'Malia was the President and guiding spirit of the corporation and he and his wife and son comprised the three man board of directors.

The Appellant submits that upon the facts found by the court the corporation became bound by the Chartrand-O'Malia agreement and that since no affirmative defenses, if any existed, were plead or proved, they were waived.

Nowhere is it contended that the corporation did not receive the entire benefit of the contract and the agreement after acceptance of the benefits cannot be altered by the unilateral action of the corporation.

The appellant has carried his burden of proof by proving the terms of the pre-incorporation contract and full compliance therewith and is entitled to fifteen additional shares of capital stock of Barney's Club, Inc.

IS APPELLEE BOUND BY DISTRICT COURT'S FINDINGS WHERE HE HAS MADE NO CROSS-APPEAL?

Appellee is apparently attempting to dispute the findings of the District Court that Barney's Club, Inc. had knowledge of the pre-incorporation agreement, which is the subject of this action. Since Appellee has not cross-appealed, this finding cannot now be reviewed on appeal. *Abel v. Brayton Flying Service* (5th Cir.) 248 F.2d 713 (1957); *Teas v. Kimball* (5th Cir.) 275 F.2d 817 (1958). Where a timely notice of cross-appeal had not been filed by appellee, the Court of Appeals for the Second Circuit refused to review the findings of the lower court even though the court was inclined to conclude that the findings lacked support in the evidence. *Schildhaus v. Moe* (2nd Cir.) 319 F.2d 587 (1963).

Even assuming that the findings below are reviewable on appeal, appellee misapprehends the nature of the amended finding of the Court below. The trial court's finding was not to the effect that since the corporation received the benefits of the pre-incorporation contract, knowledge of the contract would thereby be imputed to it. The lower court made a finding that the corporation knew of the terms of the pre-incorporation agreement between Chartrand and O'Malia because "O'Malia was the President and guiding spirit of the corporation and he, his wife and his son comprised the three man board of directors." (T. 88).

Knowledge of a promoter can be imputed to the corporation where the promoter becomes a director, officer and major stockholder of the corporation he has formed. *Wallace v. Eclipse Pocahontas Coal Co.,* 83 W. Va. 321, 98 S.E. 293; *Wall v. Niagara Mining & Smelting Co. of Idaho,* 20 Utah 474, 59 Pac. 399; *Seymour v. Association,* 144 N.Y. 333, 39 N.E. 365, 26 L.R.A. 859; *New England Oil Refining Co. v. Wiltsee,* 3 F.2d 424; *In Re Super Trading Co.,* 22 F.2d 480; *Buckman v. Bankers Mortgage Company,* Mo. App. 263 S.W. 1046; *Pleasants, et al. v. Blackberry, Kentucky & West Virginia Coal & Coke Co.,* 201 Ky. 144, 255 S.W. 1043; *In Re Quality Shoe Shoppe, Inc.,* 212 Fed. 321; *Oakes v. Cattaraugus Water Co.,* 143 N.Y. 407, 38 N.E. 461; *Lowther v. Blair Distilling Co.,* 266 Ky. 428, 99 S.W. 2d 204.

Further, the entire $80,000 specified in the pre-incorporation agreement was paid to the corporation by

Chartrand *after* it was formed. Barney O'Malia as President and Chairman of the Board of Directors, was the corporation's agent when the money was accepted. He was the "guiding spirit" of the corporation and its President and along with his immediate family, comprised the entire Board of Directors. The corporation could have refused the $80,000 and thus declined to accept the benefits of the pre-incorporation agreement had it chosen to do so. Thus, not only O'Malia's knowledge as a promoter and director of Barney's Club, Inc. must be imputed to the corporation, but also his knowledge as president and chairman of the board.

It is well settled in Nevada that knowledge acquired by an agent of the corporation is knowledge of the corporation. The court stated in *Strohecker v. Mutual Building & Loan Association of Las Vegas, Nevada,* 55 Nev. 350, 355, 34 P.2d 1076 as follows:

> "A corporation can acquire knowledge or receive notice only though its officers and agents, and hence the rule holding a principal, in case of a natural person, bound by notice to his agent is particularly applicable to corporations, the general rule being that the corporation is affected with constructive knowledge, regardless of its actual knowledge, of all the material facts of which its officer or agent receives notice or acquires knowledge while acting in the course of his employment and within the scope of his authority, and the corporation is charged with such knowledge even though the officer or agent does not in fact communicate his knowledge to the corporation."

Further evidence that the directors and officers had notice of the pre-incorporation agreement is found in one of the stipulations in the pretrial order. Paragraph 22 (T. 64) "The corporation executed Stock Certificate No. 32 in the amount of 255 shares to Richard L. Chartrand on October 3, 1960, which certificate was never delivered to Mr. Chartrand."

In *Bryan v. Northwest Beverages, Inc.,* 69 N.D. 274, 285 N.W. 689, 123 A.L.R. 717, cited in appellee's brief, one of the factors which the court stressed in deciding that the corporation had knowledge of the pre-incorporation agreement and thereby became bound by it was the fact that the corporation issued the shares of stock according to the agreement, retained them and later cancelled them.

The fact that the corporation has partially performed on the contract in question by issuing Chartrand 240 shares of stock in Barney's Club is further evidence that the corporation had knowledge of the agreement.

Another indication that the corporation had actual knowledge of the agreement is that O'Malia and his immediate family received in excess of 255 shares of the capital stock of Barney's Club, Inc. (T. 69, 70).

It is clear that the corporation had not only constructive knowledge of the Chartrand-O'Malia agreement through Barney O'Malia as a promoter, but also had actual knowledge through its directors and officers *after* the incorporation of Barney's Club, Inc.

The appellee does not deny that the corporation has received the benefit of the pre-incorporation con-

tract. See plaintiff's answer, Paragraph IV (T. 57, 58). The trial court also found in its findings of fact that the agreement was that Chartrand and O'Malia each were to contribute $80,000, and that Chartrand had in fact paid the $80,000 to the corporation (T. 68). There is no question whatsoever that Barney's Club, Inc. received the entire benefit of the contract and nowhere is it contended that this agreement was not for the benefit of the corporation.

Therefore, the corporation should be bound by the agreement under the general rule that if a corporation with knowledge of a pre-incorporation contract accepts the benefits thereof, it will be required to perform the obligations. *Murry v. Monter,* 90 Utah 105, 60 P.2d 960; *Gardiner v. Equitable Office Building Corporation,* 273 Fed. 441 (C.A. 2d) 17 A.L.R. 431; *Commercial Lumber Co. v. Ukiah Lumber Mills,* 94 C.A. 2d 215, 210 P.2d 276; *Bryan v. Northwest Beverages, Inc.,* 69 N.D. 274, 285 N.W. 689, 123 A.L.R. 717; *Ramsey v. Brooke County Bldg. & Loan Assn.,* 102 W. Va. 119, 135 S.E. 249, 49 A.L.R. 668; 4 Cook, *Corporations* (8th Ed.) Sec. 707, p. 2894.

CHARTRAND HAS SUSTAINED THE BURDEN OF PROOF THAT BARNEY'S CLUB, INC. HAS ADOPTED THE PRE-INCORPORATION CONTRACT AS ITS OWN: THE BURDEN OF PROOF IS ON APPELLEE THAT THE CONTRACT WAS DISCHARGED.

It is well known that the party seeking specific performance of a contract must prove the material facts with regard to his right to specific performance and the opposing party must plead and prove the facts

relied upon as a defense. It must be proved that there is a contract binding upon the parties and that the party seeking specific performance has fully performed or has offered to perform his part of the contract. *Bowman v. Reyburn,* 115 Colo. 82, 170 P.2d 271.

In a suit against a corporation on a promoter's contract, the burden is on the plaintiff to prove the necessary elements of his claim, among them, that the corporation received and accepted the benefits of the contract. *Glass v. Newport Clothing,* 110 Vt. 368, 8 A.2d 651. Chartrand has proved that Barney's Club, Inc. has received the benefits of the contract, namely the $80,000 which was to be paid in return for 255 shares of stock.

The corporation's knowledge of the contract has also been proved (T. 89). Therefore, appellant's burden of proof has been sustained that the corporation adopted the contract. Further, since Chartrand has fully performed his part of the bargain, he is entitled to specific performance of the 15 shares of capital stock of Barney's Club, Inc. It is not necessary for appellant to further prove that the contract has not been discharged in some manner, and the burden of any such defense shifted to the appellee. It was incumbent on the corporation to plead and prove any affirmative defenses it may have had.

The Restatement of the Law of Contracts, Vol. II, § 385, pp. 725, 726 sets out 21 methods by which a contractual duty may be discharged. Barney's Club, Inc. in its answer to Chartrand's counter-claim inter-

posed a general denial and no affirmative defense (other than the alleged settlement agreement) to the pre-incorporation contract was plead.

Rule 8 (c) of the Federal Rules of Civil Procedure requires that in answer to a pleading, estoppel, waiver or other matter constituting an avoidance or affirmative defense must be set forth affirmatively. Rule 12 (h) provides that if affirmative defenses are not plead nor made the subject of motion under 12 (b), they are waived. *Carter v. Powell* (5th Cir.) 104 F.2d 428; *Systems Incorporated v. Bridge Electronics Company* (3rd Cir.) 335 F.2d 465.

Barney's Club did not plead estoppel, waiver, novation or any other affirmative defense. It has not been set forth that there was an abandonment of the original contract or that a novation was effected thereby or that there was a rescission of the pre-incorporation agreement upon the signing of the application to the Nevada Gaming Control Board. Yet, the decision below seems to be bottomed on one or all of these points in spite of the fact that no affirmative defense was plead at all.

Assuming *arguendo,* that any one or all of the above defenses were properly plead, the question still remains whether the application to the Nevada Gaming Control Board can in some manner supersede the Chartrand-O'Malia agreement, thereby cutting off Chartrand's right to 15 more shares of stock. The *Murry v. Monter* case cited by the court below is not authority for this proposition. It is distinguishable on its facts.

Murry and Monter were both promoters of Tintic Mining Co. Murry agreed to transfer certain mining claims to Monter on the day of incorporation of Tintic in return for 120,000 shares of stock. At the time, it was contemplated that the corporation would issue 2,000,000 shares of stock and each of the subscribers would receive a certain number of shares. At the time of incorporation, the decision was made to cut the authorized capital stock in half, or to issue only 1,000,000 shares. Thereafter, each of the incorporators received the same percentage of stock for which he had subscribed, although each received half the number of shares as originally contemplated. The articles of incorporation were were signed by Monter and Murry and three others, as incorporators, provided for 1,000,000 shares of stock, 300,000 of which would be issued to the subscribers, of which Murry subscribed 60,000 shares. The articles recited that the subscriptions were paid in full by the transfer of various mining claims. At the same time, Murry transferred all the property, which was the subject of the contract, to the corporation by deed. Nothing was said at this time or at any later meeting of the Board of Directors, of which Murry was a member, that he had a right to more than 60,000 shares. Several months later, Murry demanded the remaining 60,000 shares from Monter. The holding of the court in that case was distinguishable in this fashion.

First, it was held that this was a secret agreement between Murry and Monter. None of the other three incorporators had any knowledge of the contract and

further, that the corporation had no knowledge of it. Therefore, the corporation could not be said to have adopted the agreement by accepting the benefits of the contract with knowledge of its terms.

Secondly, although it was specifically pleaded that Murry's signing the articles of incorporation, wherein he agreed to deed his interest in the claims for the 60,000 shares, which was inconsistent with the prior contract, resulted in a rescission, a waiver and an abandonment of the original contract, the court rejected that argument. It stated that such a defense pre-supposes that the corporation would be liable on the promoter's contract, but since the corporation had no knowledge of the contract, it had not adopted it. Therefore, the only contract binding upon the corporation was the one evidenced by the articles of incorporation, wherein Murry agreed to convey his interest in the mining claims for 60,000 shares of stock subscribed.

The third and probably most important argument was that *Murry received the exact proportion of ownership in Tintic corporation as he had bargained for.*

In the case at bar, the resolution to issue Chartrand 240 shares was made by a Board of Directors comprised of O'Malia, his wife, and his son. O'Malia was the president and guiding spirit of Barney's Club, Inc. (T. 88). The mere signing of the application to the Gaming Control Board affirming that 240 shares of stock had been issued to him does not in any sense "ratify" a decision by the Board of Directors (domi-

nated by O'Malia) not to issue an additional 15 shares. Chartrand has repeatedly demanded the additional 15 shares of capital stock of Barney's Club, Inc. in conformity with the pre-incorporation contract (T. 70).

Appellee cannot now attempt an affirmative defense by inference or implication which he has not plead or proved.

SHOULD APPELLEE BE ALLOWED TO UNILATERALLY CHANGE OR MODIFY THE PRE-INCORPORATION AGREEMENT AFTER APPELLANT HAS FULLY PERFORMED HIS PART OF THE CONTRACT?

No abrogation, change, modification, or substitution in a primary contract can be effected by the sole action of one of the parties to it. The consent of both is required to cancel, alter, or supplant a contract fairly made. The same meeting of the minds is needed that was necessary to make the contract in the first place. Consideration is also required. *H. Horowitz v. Weehawken Trust & Title Co.,* 10 N.J. Mis. R. 417, 159 A. 384; *Wheeler v. New Brunswick & C.R. Co.,* 115 U.S. 29, 5 S. Ct. 1061; *Holland v. Crummer Corp.,* 78 Nev. 1, 368 P.2d 63.

> "A person shall not be allowed at once to benefit by and repudiate an instrument, but, if he choose to take the benefit which it confers, he shall likewise take the obligations or bear the onus which it imposes . . ." *Alexander v. Winters,* 23 Nev. 475, 486, 49 Pac. 116.

> "One Party cannot, while he retains the benefit of a substantial performance, totally defeat an action for the price which he agreed to pay, or for specific performance on his part, on the ground that the plaintiff has not completed the contract. He cannot at the same time affirm the contract by retaining its benefits and rescind it by repudiating its burdens. The reason for this principle is that the retention of the benefits of a substantial performance after a default is utterly inconsistent with the position that the default has released the party who has received these benefits, so that he is not bound to perform his part of the contract." *Turley v. Thomas,* 31 Nev. 181, 193, 101 Pac. 568, citing *German Sav. Inst. v. De La Vergne R. M. Co.,* 70 Fed. 146, 17 C.C.A. 34.

Barney's Club is bound to perform its part of the contract after having received the entire consideration from appellant.

APPELLANT ACKNOWLEDGES THAT HE IS BOUND BY THE FINDINGS OF FACT MADE BY THE TRIAL COURT.

The appellant acknowledges that he, as well as appellee, is bound by the Findings of Fact and all facts which are included in the Conclusions of Law which are not included in the Findings of Fact made by the court below. It is from these findings that the appellant contends that the corporation adopted the agreement and is bound thereby to full performance.

CONCLUSION

In view of the foregoing the decision of the lower court denying equitable relief to the appellant should be reversed and the trial court directed to deliver to appellant Chartrand an additional fifteen (15) shares of stock of Barney's Club, Inc. and all of the incidents thereof.

Dated, Reno, Nevada,
October 17, 1966.

Respectfully submitted,
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CERTIFICATE OF COUNSEL

We certify that, in connection with the preparation of this brief, we have examined Rules 18 and 19 of The United States Court of Appeals for the Ninth Circuit, and that, in our opinion, the foregoing brief is in full compliance therewith.

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